To: Natalia Vera, ABA Center for Professional Responsibility

From: Christopher Davis, Executive Director, International Cannabis Bar Association (INCBA)
Jessica McElfresh, Chair, Professional Responsibility and Ethics Committee, INCBA
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Date: February 15, 2022

Re: Request by ABA Standing Committee on Ethics and Professional Responsibility and ABA Standing Committee on Professional Regulation for Comments on Proposed Amendments to Model Rule Comments Relating to Lawyers' Due Diligence and Money Laundering

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In its December 15, 2021 Memorandum (Memo), the ABA Standing Committees on Ethics and Professional Responsibility and Professional Regulation (Committees) requested comments to possible amendments to the Comments of the ABA Model Rules of Professional Conduct (Model Rules). The amendments are a response to urging from *inter alia* the Financial Action Task Force (FATF) and the United States Government (including the Department of Treasury) "to create an enforceable client due diligence obligation in the Model Rules" or else face "increased federal legislative and regulatory action."

INCBA's purpose is to make the practice of law more secure through its efforts to educate lawyers about the ethical, professional, legal implications of practicing law within the regulated cannabis industry throughout the world, including the 38 U.S. states that have implemented medical cannabis programs.

The implementation of client due diligence requirements related to Anti-Money Laundering (AML) and Bank Secrecy Act (BSA) is a laudable goal and should be designed to bring these Model Rules into accordance with FATF recommendations to promote adoption in US Jurisdictions.

Nevertheless, we fear that the unintended consequences of the proposed comments will force states that have implemented adult-use and medical cannabis regulatory regimes to decline to adopt this guidance, as it discourages or denies legal services to those in the state-legal adult and medical cannabis industry.

Indeed, BSA and AML programs are key aspects of most, if not all, state-level cannabis regulatory regimes, and lawyers play a primary role in guiding clients towards compliance. The promulgation of language that does not address the conflict between federal and state law and deprives cannabis-industry market participants of legal counsel runs contrary to the stated goals herein of having the legal profession support BSA and AML compliance.

Moreover, the broad language ignores many high-risk industries and activities that remain federally legal or gray. NFTs and other crypto-currency tools have become increasingly popular, and it has become clear that certain activities that are illegal under traditional securities laws may be widely used in the NFT market to manipulate prices and possibly launder money.[1] However, given the uncertain legal status of NFTs as securities, these activities may not trigger traditional securities laws, excluding them

[1] https://www.nbcnews.com/tech/security/nft-sales-show-evidence-wash-trading-researchers-say-rcna14535

from withdrawal requirements related to illegal activity proposed here. It is therefore our belief that this guidance is both over and under-inclusive to achieve its stated goal.

On behalf of INCBA's Professional Responsibility and Ethics Committee, I submit the below two comments for consideration by the Committees.

Comment No. 1. The scope of the proposed amendments exceeds their stated purpose.

The stated reason for the Memo's suggested amendments is to increase lawyer-client due diligence obligations in order to address concerns about the lawyer's role in BSA and AML violations; however, the language is too broad.

The proposed comments to Rule 1.1 require the lawyer to make a reasonable inquiry, and "decline or terminate the representation when the lawyer has reason to believe that the client seeks the lawyer's services in criminal or fraudulent activity." Similarly, the proposed comments for Rule 1.2 states that, "[a] lawyer may not knowingly assist in criminal or fraudulent activity and should discourage a client from engaging in such activity, but the lawyer may offer to assist in achieving the client's lawful objectives by lawful means[]" and requires a lawyer to withdraw from representation if the lawyer has knowledge of criminal activity.

The proposed language is overly broad because it fails to acknowledge robust industries that operate under strict state or tribal regulation but that may remain illegal under federal law. The commercial sale of medical or adult--use cannabis is legal under the laws of 38 states (and within Washington D.C.), and is anticipated to generate over $22 Billion in revenue in 2022. Yet, under federal law, cannabis remains a Schedule I drug, illegal for all purposes – including medical use.

The proposed language prohibits lawyers from representing cannabis-industry market participants – and could even create barriers for attorneys who represent state and local governments that license operators, or that accept fees or tax payments from those operators. This would be true even where cannabis is subject to a statewide regulatory scheme that contemplates lawyer involvement and guidance, and even when the individual lawyer supports BSA and AML compliance for the client at both the state and federal level.

Notably, both Congress and various federal agencies have responded to the conflict between state and federal law with legislation and guidance that enables these state markets to persist. The Rohrabacher-Farr Amendment, an annual rider to the federal appropriations bill, prohibits the U.S. Department of Justice from using any federal funds to interfere with the implementation of state medical cannabis laws.[2] The 2014 FinCEN memo permits banks to serve cannabis-industry market participants without running afoul of BSA and AML laws,[3] and substantial caselaw related to Internal Revenue Code section 280E lays out the taxpayer requirements for those engaged in federally illegal activities.

The US Congress, the US Department of the Treasury, and the IRS all agree that this inquiry into BSA and AML compliance requires an analysis of the individual client and their specific financial activities, rather than a cursory reference to the client's industry itself.

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[2] See Section 531, https://www.congress.gov/bill/117th-congress/house-bill/4505/text
[3] https://www.fincen.gov/sites/default/files/shared/FIN-2014-G001.pdf

We also note that without a *de minimis* threshold, or an explanation of the type of illegality that requires withdrawal by the attorney, this obligation, as written, potentially goes far beyond the unintended consequences outlined here.

If adopted, states will be forced to 1) implement state level cannabis markets without attorney support; 2) decline to adopt this guidance; or 3) adopt this guidance with a caveat – all of which would inhibit wide and consistent adoption of these rules.

We would propose one of two changes to the language:

1) Remove the reference to "illegal activity" and replace it with an affirmative obligation to execute diligence on the client to ensure that the lawyer is not being used as an instrumentality for BSA and AML violations.
2) Replace the prohibition on representing those engaged in illegal activity with an "also advise" position: one that requires that, when a client is clearly engaging in activity that is state or tribal-legal and federally illegal, the lawyer "also advise" on the potential consequences under federal law of that course of action, limited in scope by the scope of representation.

We recognize that a black-letter rule change is beyond the scope of these comments, but we encourage the ABA to integrate the above changes into the text of Model Rule 1.2(d) as soon as practicable.

Comment No. 2. The Memo has the unintended consequence of amplifying conflicts among States' ethical standards, rather than promoting uniformity. *This threatens the ability of the profession to continue to self-govern.*

Lawyers recognize the importance of self-governance, uniformity of rules across jurisdictional lines, and consistency of rule application, especially for those of us that practice law in multiple states. By proposing language inconsistent with the legislative actions of 38 US States, this proposed language threatens to further fracture the ethics rules governing the legal profession and roll back the substantial progress towards uniformity and consistent application of ethics rules that has been at the forefront of these Committees' work.

Rule 1.2(d) and its conflict with the cannabis industry has prompted many state bars to either: 1) change their ethics rules to allow for the practice of law in the cannabis industry; or 2) prohibit access to lawyers for the implementation of complex regulatory systems, inviting the legislature to step in and pass laws regulating the conduct of lawyers to help realize their vision of a regulated cannabis market.

In Alaska, Arizona, Colorado, California, Massachusetts, and many others, Rule 1.2(d) (in whatever form it was adopted) has been augmented with language clarifying that lawyers may advise the clients on state level regulatory regimes despite federal illegality, as long as the attorney also advises on the consequences to the client under federal law.[4]

[4] https://resources.incba.org/cannabis-attorney-resources/state-by-state-ethics-rules-for-cannabis

In some states, including Michigan, the state bar has taken no position, and the Supreme Court has yet to weigh in – leaving our colleagues in ethical limbo as they attempt to help implement the state's mandated cannabis regulatory regime.

In other states such as Georgia, state bars have proposed amendments to the ethics rules to allow cannabis practice, only to have the state Supreme Court strike down the amendment. Georgia continues to implement its medical cannabis program, and each and every one of the lawyers helping push their clients into properly regulated channels – and helping them comply with BSA and AML rules – is now at substantial risk of professional sanction. To solve this problem, the state legislature may be drafting a new set of mandated protections for lawyers.

These Committees hold sway with state bars and state supreme courts and have the ability to preempt state legislatures to maintain the self-regulatory nature of our profession. It is critical that we eliminate language that forces states to take power away from our state bars in favor of the legislature. To that end, we urge these Committees to adopt a proposal that is narrowly tailored to achieve the laudable goals of BSA and AML compliance, without prohibiting lawyers from helping the very clients that need our services the most.

We thank the Committees for their hard work, their dedication to the legal profession, and for the substantial time and energy contributed to better establish lawyers' responsibilities to our clients, the courts, and the law of the land. Please do not hesitate to reach out with additional questions, we are here to support your efforts.